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TREASURY FOR U/S TAYLOR AND OASIA - MILLS
NSC FOR QUANRUD AND BRYZA

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SUBJECT: TURKISH ECONOMY APRIL 3: MARKETS LIKE SECRETARY'S
VISIT, BUT STILL WARY OF AK

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Well Timed Market Bounce From Secretary's Visit

11. (U) Positive local press coverage of the Secretary's April 3 visit translated into a modest bounce in local financial markets, well timed in advance of key large April 8 debt auctions. Market analysts told us the Secretary's affirmation of the bilateral relationship was helpful to general sentiment. The lira strengthened about one percent in morning trading to TL 1,675,000 to the dollar. T-bill yields dropped nearly two percentage points to 63 percent compounded. The Istanbul Stock Exchange rose 2.2 percent in morning trading.

12. (U) On April 3, Deputy Treasury U/S Hakan Ozyildiz explained Treasury's strategy for the April 8 debt auctions. IMF management had approved the LOI on evening of April 2; MinState Babacan and Treasury U/S Oztrak were in Istanbul meeting with banks and would coordinate with the Central Bank on signing the LOI. Treasury would let the local banks digest the good news of the LOI signing, and then check on their appetites for new T-bill instruments. Once Treasury had updated feedback from the local banks, it would announce the bills to be issued on April 8. Ozyildiz foresees issuing two lira T-bills, both a short and longer-term maturity.

Market Sentiment Towards AK Remains Negative

13. (SBU) Treasury Deputy U/S Ozyildiz (protect) added that despite the good news of U.S. and IMF support, markets remain highly skeptical of AK's intentions of implementing economic reforms. He also noted recent unhelpful press rumors of imminent changes at Treasury (e.g., Finance Minister Unakitan's comment that Treasury might be folded into the Finance Ministry; ongoing press speculation that U/S Oztrak will be replaced). Comment: Ozyildiz's view is not objective, since he might be replaced if Oztrak goes. However, he is accurately summing up market attitudes towards AK. Recent state bank and state energy company personnel changes (septel on latter) have done nothing to dispel such attitudes. As one Turkish investor told us, Babacan's mid-March statements intentionally misleading markets about the status of the original U.S. package would in other countries have led to criminal charges. End Comment.

14. (SBU) Negative feelings for AK notwithstanding, market participants tell us they plan to roll-over the debt on April 18. Looking beyond the April debt auctions, the key problem is the ongoing high real interest rates (about 32 percent) demanded for such roll-overs. Given the short maturity of the TL debt, these real rates require Turkish banks to maintain and increase if possible their current liquidity levels. At present, it appears that many banks do have extra lira liquidity, sitting in the money markets, that could be used to roll-over the ever increasing amount of T-bills. But F/X liquidity has recently been a problem for Turkish banks (liquidity is fungible). And reducing real rates, dependent on the GOT restoring confidence via strongly implementing reforms, may take months, if it happens at all. In this atmosphere of uncertainty and lack of confidence in the GOT, maintaining the inter-bank lines of credit will be critical to GOT solvency.

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